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In the Supreme Court of the United States

October Term, 1981

WILLIAM L. GUNTER and CAMILLE S. GUNTER,
Petitioners,

vs.

THEODORE M. HUTCHESON *et al.*,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1.

When innocent victims are concededly defrauded in a stock transaction involving a bank, which bank subsequently falls into receivership and liquidation administered by the Federal Deposit Insurance Corporation (FDIC), must there be a new rule of federal common law that cuts off the rights victims would otherwise have to a trial under state antifraud statutes and case law?

2.

Do conceded victims of a bank's securities fraud lose their rights under the federal securities laws to resist the fraudulent transaction in court when the FDIC takes over the bank and transfers the

victims' note from the FDIC "as receiver" to the FDIC "as liquidator"?*

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* The following were parties to the proceeding in the court of appeals: William L. Gunter; Camille S. Gunter; Theodore M. Hutcheson; N. Rountree Youmans; Philip S. Barrett; T. Wendell Holliday; Marion H. Hutcheson, W. Frank Hutcheson, Marion H. Hutcheson, II, and Virginia Gill as Executors of the Estate of John L. Hutcheson, Jr.; Hugh S. Hauck; B. Lamar Rankin; James T. Vann; Paul R. Cobble; Richard A. Chepul; Thomas F. Mahone; W. Frank Hutcheson; and the Federal Deposit Insurance Corporation.

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PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT
OF APPEALS
FOR THE ELEVENTH CIRCUIT

William L. Gunter and Camille S. Gunter respectfully petition that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Eleventh Circuit entered in this proceeding on April 30, 1982.

OFFICIAL REPORTS

The district court opinions are reported at 492 F. Supp. 546; the court of appeals opinion has not yet been reported.

STATEMENT OF JURISDICTION

The judgment of the court of appeals was entered on April 30, 1982. This petition was filed within ninety days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES AND REGULATION

This proceeding involves the following statutes and regulation, which because of their length, are set forth in the Appendix: 12 U.S.C. § 1823(e), 15 U.S.C. §§ 77q, 78j, 78cc(b) and (c), and 17 C.F.R. § 240.10b-5.

STATEMENT OF THE CASE

I. Summary

Mr. and Mrs. William Gunter bought stock in a bank in the Hamilton system of banks (which operated in Georgia and Tennessee) shortly before that banking system fell into bankruptcy and liquidation by the Federal Deposit Insurance Corporation (hereinafter, "FDIC"). For purposes of this review, the FDIC concedes the Gunters were defrauded. Appendix, pp. A8, A90. Accordingly, the Gunters' claims that they were told the Hamilton system was sound and had sound management have been admitted as true for this Court's purposes.

In the course of the transaction in which the Gunters were defrauded, they gave a $3 million note to the Hamilton National Bank of Chattanooga, Tennessee (herein-

after, "Chattanooga Hamilton"). When the FDIC took over that bank, it acquired the Gunters' note. Without having endorsed the note or having physically moved it, the FDIC now claims to have transferred the note from itself "as receiver" to itself "as liquidator," and thus to have cut off the Gunters' right to a trial at which the Gunters could present their evidence of securities fraud.

The district court and court of appeals found it necessary to create a new rule of federal common law to reach a result in favor of the FDIC and ordered summary judgment against the Gunters. In this petition, the Gunters ask this Court to review the ruling of the court of appeals.

II. How the Gunters Were Defrauded and How the FDIC Obtained the Gunters' Note

In December 1974, the Gunters purchased 61 percent of the outstanding common stock of the Hamilton Bank & Trust Company

of Atlanta, Georgia (hereinafter, "Atlanta Hamilton") for $5.5 million. The Chattanooga Hamilton financed the transaction, taking two promissory notes from the Gunters -- one for $3 million and one for $2.5 million. In the course of that transaction, Mr. Gunter was told by the chief executive officer of the Chattanooga Hamilton that the Hamilton Bancshares System was in sound condition, and that the Atlanta Hamilton had sound management.

A little over a year later, at the close of business on February 16, 1976, the Chattanooga Hamilton collapsed and the FDIC became receiver of the bank. The Hamilton Bancshares holding company fell into bankruptcy within a few days. The FDIC immediately solicited bids for a purchase and assumption transaction by which the winning bidder would purchase some of the Chattanooga Hamilton's assets and assume some of

its liabilities. The First Tennessee National Bank (hereinafter, "First Tennessee") submitted the best bid, which the FDIC accepted, and the Chattanooga Hamilton's offices opened the following morning under the First Tennessee name.

Under the provisions of the purchase and assumption agreement, all the closed bank's deposits and many of its assets were transferred to First Tennessee. Also under that agreement, First Tennessee could and did refuse some assets at the outset and did return others at a later date. The refused or returned assets were therefore left to the FDIC to administer. Appendix, pp. A88-A89.

The Gunter notes were among the assets transferred to First Tennessee as part of the purchase and assumption transaction. Pursuant to its rights under the purchase and assumption agreement, First Tennessee

later returned those notes to the FDIC. Appendix, p. A89. The FDIC, acting as receiver, then apparently transferred the $3 million note to itself, acting as liquidator of the Chattanooga Hamilton. The FDIC did not endorse or physically move the note. That transfer apparently was accomplished pursuant to an "Agreement of Sale" executed on the night the bank closed, which agreement purported to sell to the FDIC as liquidator all assets not accepted by First Tennessee. Id.

Later the same year, on October 8, 1976, the Atlanta Hamilton was also declared insolvent. That same month, the Gunters filed this suit against a number of defendants, including former directors and officers of the Chattanooga Hamilton, and the FDIC. Insofar as the FDIC is concerned in this proceeding, the Gunters' suit seeks rescission and return of the $3 million

note under federal and state securities laws, and under the common law.

The FDIC counterclaimed for enforcement of the $3 million note and moved for summary judgment on the theory that 12 U.S.C. § 1823(e) and federal common law protect the FDIC against the Gunters' claims and defenses of fraud. As the court of appeals recognized, "[f]or the purposes of the summary judgment motion, the FDIC agreed that the Gunters were defrauded into their stock purchase and that this fraud ordinarily would be adequate grounds for rescission." Appendix, p. A90.

III. Lower Court Rulings

Jurisdiction in the district court was based upon (1) the provisions of Sections 22(a) and 17 of the Securities Act of 1933, as amended, 15 U.S.C. §§ 77v(a) and 77q, respectively; (2) Sections 27 and 10(b) of the Securities Exchange Act of

1934, as amended, 15 U.S.C. §§ 78aa, 78j(b), respectively, and the Rules and Regulations of the Securities and Exchange Commission, including Rule 10b-5, 17 C.F.R. § 240.10b-5; (3) the doctrine of pendent jurisdiction; and (4) 1966 Ga. Laws, p. 343 and 1970 Ga. Laws, pp. 443, 444 (Ga. Code Ann. § 24-113.1).

The FDIC moved for summary judgment, primarily on the basis of 12 U.S.C. § 1823(e), which protects the FDIC against unwritten "side agreements" made by a failed bank. The motion contained no mention of federal common law (neither, for that matter, did the FDIC's Answer).

The district court granted the FDIC's motion, holding that, although 12 U.S.C. § 1823(e) did not protect the FDIC against the Gunters' claims and defenses of fraud, a new rule of federal common law provided the FDIC with a defense to claims of fraud

of which it lacked knowledge. Alternatively, the district court ruled that the Gunters' federal securities laws claims against the FDIC were barred by Section 29(c) of the Securities Exchange Act, 15 U.S.C. § 78cc(c).

The district court granted certification of its decision for interlocutory appeal under 28 U.S.C. § 1292(b), finding that the decision was essentially final, but further finding that requiring the Gunters to post a bond would be unfair in view of the new common law being made. The court of appeals granted permission to appeal.[1]

Affirming the decision of the district court, the court of appeals held that: (1) the statutory language of 12 U.S.C. § 1823(e) does not bar the Gunters' claims

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[1] For practical purposes, the lower court decisions are thus final, despite the technically interlocutory stance of the proceeding. See Appendix, pp. A72-A79.

and defenses of fraud; (2) under a new rule of federal common law, the FDIC has a complete defense to the Gunters' state and common law fraud claims; and (3) Section 29(c) of the Securities Exchange Act precludes the Gunters' claims and defenses of fraud under both the Securities Exchange Act and the Securities Act.

ARGUMENT

I. The Issues Surrounding Insulation of the FDIC Are Recurring Frequently in the Circuits With Divergent Results.

On at least five occasions in the last two years, the various circuits have faced the battle between the FDIC and a person seeking to resist a transaction with a closed bank. No case has come out the same way on the same rationale as any other such case. Compare Gilman v. FDIC, 660 F.2d 688 (6th Cir. 1981) (bona fide purchaser concept); FDIC v. Lattimore Land Corp., 656

F.2d 139 (5th Cir. 1981) (fraud claims reworked into side agreements and cut off under § 1823); Black v. FDIC, 640 F.2d 699 (5th Cir.), cert. denied, 102 S. Ct. 143 (1981) (§ 1823 applies because claim amounts to assertion of failure of consideration); FDIC v. Waldron, 630 F.2d 239 (4th Cir. 1980); and Gunter v. Hutcheson, No. 81-7129 (11th Cir. Apr. 30, 1982) (new rule of federal common law) (reprinted in Appendix, beginning at p. A82).

Not since 1942 has this Court addressed the FDIC's insulation from claims by those involved in transactions with closed banks, and the then-recent federal securities laws were not a factor in that case. D'Oench, Duhme & Co. v. FDIC, 315 U.S. 447 (1942).

The unsettled state of the existing law becomes most apparent in comparing the Eleventh Circuit law, represented by the

instant case, to the Ninth Circuit law in FDIC v. Meo, 505 F.2d 790 (9th Cir. 1974). The defendant in Meo, as in the case at bar, had executed a promissory note to a national bank which later collapsed into FDIC receivership. As in the case at bar, the note was given as part of a sale of stock. When the FDIC sought to enforce the note, the defendant asserted failure of consideration as an affirmative defense.

The FDIC argued in Meo that this Court's decision in D'Oench, Duhme & Co. v. FDIC, 315 U.S. 447 (1942),[2] "stands for the broad proposition that FDIC and the depositors it represents are protected from losses due to reliance upon the notes of insured banks which are later subject to the claim of some undisclosed defenses."

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[2] The district court in its March 4, 1981 Order recognized Meo as "the leading D'Oench progeny." Appendix, p. A56 n.7.

FDIC v. Meo, 505 F.2d 790, 792 (9th Cir. 1974). The Meo court rejected that argument, finding that D'Oench stands only for the very narrow proposition that the accommodation maker of a note may not take advantage of an undisclosed and fraudulent arrangement which public policy condemns, and which the maker of the note made possible. Since the Meo defendant was a wholly innocent purchaser/borrower, the court refused to make him "an insurer of financial representations of the bank with whom he conducts business," and held that he was not estopped from asserting the defense of failure of consideration against the FDIC. FDIC v. Meo, 505 F.2d 790, 793 (9th Cir. 1974).

Meo and this case present the same conflict of policies. Although Meo involved no "purchase and assumption" agreement, the policy in favor of such agree-

ments does not truly arise in this case.[3] Indeed, the Gunters' position vis-a-vis the FDIC is practically the same as the defendant's in Meo. Like that defendant, the Gunters are bona fide borrowers who are victims of a bank's wrongful conduct in a securities transaction; they are assumed to be completely innocent of any wrongdoing or negligence, and not to have lent themselves to any agreement or arrangement likely to mislead the FDIC. Since the Gunters are victims of fraud, the holding of the court of appeals, which would make them insurers of the bank with whom they did business, seems particularly harsh and in conflict

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[3] Even the court of appeals implicitly recognized that, because of the similarity of the two cases, the court's holding is at odds with the Meo decision to some extent. The court of appeals stated that "Meo is not directly contradictory to our holding." Appendix, p. A136 n.15 (second emphasis added). In fact, the holdings are as nearly in direct conflict as is likely to occur in any area of the law.

with Meo.[4] In fact, the Meo rationale is even more compelling in this case, because the Gunters assert not merely failure of consideration, but actual securities fraud.

II. The Conflict Between the FDIC's Professed Need for Legal Insulation from Claims (Under the FDIC Act) and the Rights of Conceded Victims of Securities Fraud (Under the 1933 and 1934 Acts and State Law) Presents an Important Issue, Which This Court Ought to Decide.

As victims of the kind of fraud the federal securities laws were designed to remedy, the Gunters undoubtedly would be

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[4] The Meo decision also highlights the tension between the decision of the court of appeals in this case and the decision of this Court in D'Oench. The court of appeals acknowledged that the policy embodied in D'Oench protects the FDIC only "in a more limited manner" than the rule of federal common law which the court of appeals adopted. Appendix, p. A111. Nevertheless, unlike the Ninth Circuit in Meo, the court of appeals in this case refused to be bound by the narrow parameters of D'Oench, finding instead that D'Oench "provides a general basis for a federal policy to protect the FDIC" from defrauded note-makers like the Gunters. Appendix, p. A135 n.14.

entitled to assert such fraud to resist enforcement of their note by the bank that defrauded them. 15 U.S.C. § 78cc. Indeed, the FDIC conceded for purposes of its motion "that all the Gunters' factual assertions of fraud are true." (R. 2390.) Consequently, the district court treated as established the existence of "fraud and violations of the securities laws and plaintiffs' entitlement to recover." (R. 1719.)

The lower courts found that the need to protect the FDIC outweighed the Gunters' "entitlement to recover" under the Securities Act of 1933,[5] the Securities Exchange Act of 1934, and state statutory and common law regarding securities fraud.

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[5] The Gunters rely upon Section 17 of the 1933 Act primarily by way of defense rather than as an affirmative right of action. This Court's review would thus not necessarily address the question of whether there is an implied private right of action under that section.

Stepping back a few steps to gain perspective, we may see in this case a conflict between two powerful policies. On the one hand, we have a policy of aiding the FDIC through some insulation from claims by noteholders (although the FDIC apparently did not count on such insulation when it acquired the Gunter note in this case).[6] On the other hand, we have the policy -- long recognized by this Court as extremely important[7] -- of allowing victims of securi-

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[6] The FDIC now says it relied upon the Gunters' note being worth its face value in choosing a "purchase and assumption agreement" over a straight "payout." Yet, the FDIC never showed that it relied upon the Gunter loan's being sound in deciding whether to choose a purchase and assumption agreement. In fact, the Gunter loan was in default as to interest when the FDIC took over the Chattanooga Hamilton, and the FDIC expressly noted the possibility that First Tennessee might return the Gunter loan as unacceptable, which that bank did.

[7] See, e.g., Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972); Deckert v. Independence Shares Corp., 311 U.S. 282 (1940); Strong v. Repide, 213 U.S. 419 (1909).

ties fraud a trial. The court of appeals in this case resolved the conflict in favor of the FDIC.

One might have thought the decision would come out the other way. For hundreds of years, the law has recognized that persons claiming fraud at least should have a day in court.[8] Similarly, for at least that long, the law has recognized that a transfer of a contract does not ordinarily in-

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[8] Actions for fraud and deceit are as old as recorded law, dating back at least as early as 1201. See 1 Street, Foundations of Legal Liability 375 (1906); W. Prosser, Handbook of the Law of Torts 685 (4th ed. 1971).

sulate the transferee from such claims,[9] even in a bank's collapse.[10]

In this case, however, the lower courts resolved the conflict in favor of the FDIC. To do so they had (1) to develop a new rule of federal common law with vary-

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[9] For centuries, Anglo-American case law has reflected the principle that a transferee of rights under a contract acquires no greater right than his transferor had. That was sometimes expressed in the maxim nemo plus juris ad alium transferre potest, quam ipse habet ("no man can transfer more right to another than he has himself"). See, e.g., Withers v. Greene, 50 U.S. (9 How.) 213 (1850); Ventress v. Smith, 35 U.S. (10 Pet.) 161 (1836); Davis v. Austen, 30 Eng. Rep. 325 (1790). Indeed, pages 2448-49 of the Record demonstrate the universality of the rule of federal and state common law, American statutory law, English common law, and of our Western civilization generally.

[10] The Ninth Circuit reflected that principle in FDIC v. Meo, 505 F.2d 790, 793 (9th Cir. 1974), where it quoted Mr. Justice Jackson's language from D'Oench that ordinarily "the FDIC succeeds only to the rights which the bank itself acquired." The law has long recognized that bank failures do not make holders in due course of those who acquire the failed bank's paper. See, e.g., Baach v. Bank of Pocahontas, 157 Va. 274, 160 S.E. 68 (1931); Ward v. Oklahoma State Bank of Atoka, 51 Okla. 193, 151 P. 852 (1915); Middle Tenn. Bank v. McKennon, 20 Tenn. App. 416, 99 S.W.2d 564 (1936).

ing dimensions,[11] (2) to make the FDIC into a good-faith purchaser under Section 29 of the Securities Exchange Act of 1934 (15 U.S.C. § 78cc(c)(2)), and (3) to use that "purchaser" immunity in the 1934 Act, (which limits its application to that act), to cut off rights under the 1933 Securities Act, which contains no such immunity.

Each of those three decisions demonstrates the extent to which the lower courts had to stretch the law in order to find in favor of the FDIC:

First, the creation of a new rule of federal common law obviously represents a dramatic step by any court. This Court's own last venture in that direction produced a careful decision to apply state law as a matter of federal choice. United States v.

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[11] The district court thought the new rule ought to cover all claims. The court of appeals thought it should cover only state and common law claims. Appendix, p. A121.

Kimbell Foods, Inc., 440 U.S. 715 (1979). It is difficult to understand how the FDIC, in enforcing a contract made under state law, and in relying at least in part on state law rights,[12] needs a new rule of federal common law more than any other insurance company that routinely deals at least in part under state law.

Second, the lower courts held that the FDIC's intracorporate transfer of the Gunters' note from itself as "receiver" to itself as "liquidator" was so imbued with substance as to be a transaction by which the FDIC "acquired" (albeit from itself) the note under the insulating provisions of Section 29(c)(2) of the 1934 Securities

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[12] The FDIC, as a predicate to seeking to enforce the Gunters' note, sent notice prescribed by state law, citing that state law, and claimed in its counterclaim to be claiming as a "holder" in the language of the state's enactment of the Uniform Commercial Code.

Exchange Act. Research has revealed no other decision stretching Section 29(c) so far as to say that such paper-shuffling cuts off the rights of conceded victims of securities fraud. Indeed, one would not ordinarily think such a transaction outside a normal commercial context would be the stuff of which exceptions to statutory remedies are made, particularly under the federal securities laws. See Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976); Forman v. Community Services, Inc., 366 F. Supp. 1117, 1130-32 (S.D.N.Y. 1973), rev'd, 500 F.2d 1246 (2d Cir. 1974), rev'd, 421 U.S. 837, 849 (1975) ("Congress never intended to stretch the scope of the securities acts outside the commercial world"); Securities & Exchange Comm'n v. Koscot Interplanetary, Inc., 365 F. Supp. 588 (N.D. Ga. 1973), rev'd on other grounds, 497 F.2d 473 (5th Cir. 1974) (form to be disregarded for

substance and economic realities to be emphasized); 78 Cong. Rec. 7866 (1934) (remarks of Rep. Maloney).

As the FDIC's counsel admitted before the district court, the FDIC's transfer from itself as "receiver" to itself as "liquidator" was not an ordinary commercial transfer. Appendix, p. A57 n.11. Thus, the so-called transfer should not insulate the FDIC under a statute written to benefit those making acquisitions in commercial settings. This is especially so where, as here, expanding Section 29(c) of the 1934 Act beyond its proper commercial context effectively diminishes the protection the securities laws afford to the individuals they were designed to benefit. Such a diminution of protective scope contravenes the established principle that the securities laws must be construed liberally to effectuate their remedial purposes.

Tcherepnin v. Knight, 389 U.S. 332, 336 (1967); Spector v. L Q Motor Inns, Inc., 517 F.2d 278, 286 (5th Cir. 1975), cert. denied, 423 U.S. 1055 (1976).

Third, the court of appeals found that to decide in favor of the FDIC, the court had to extend Section 29(c) of the 1934 Securities Exchange Act also to cut off rights against transferees under the 1933 Securities Act, which contains no such cut-off. The court of appeals held that such protection spills over into the 1933 Act despite a straightforward provision in the 1934 Act's Section 29(c) that its insulating provisions apply to "this chapter" -- the two acts being in separate chapters. The Congress had specifically rejected the course chosen by the court of appeals. (Although the initial draft of the 1934 Act would have allowed the 1934 Act's insulating provisions in Section 29(c) to spill

over into the 1933 Act, the 1934 Act, as passed, did not allow such a spill-over. See S. 3420, 73d Cong., 2d Sess., 78 Cong. Rec. 8588, 8600 (1934).)

The lower court's interpretation of the statute contradicts in principle the decision of this Court in City of Milwaukee v. Illinois, 451 U.S. 304 (1981). In finding that "[n]othing in this chapter" (i.e., the Securities Exchange Act) does not mean what it says, the court of appeals apparently ignored this Court's opinion in City of Milwaukee that a statute should be read "as written," because "Congress knows how to say 'nothing in this Act' when it means to." City of Milwaukee v. Illinois, 451 U.S. 304, 329 n.22 (1981).

CONCLUSION

This Court should provide guidance to the lower courts in this important area of

the law. The FDIC's purported need for insulation from claims when it takes over a failed bank is surely deserving of serious consideration. Here, however, that policy conflicts with the policy of according innocent victims of securities fraud their day in court.

Where such important policies conflict so dramatically as they do here, this Court should accept review.

Respectfully submitted,

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May 14, 1982